Fair Political Practices Commission
MEMORANDUM

To: Chairman Getman, Commissioners Downey, Knox, Scott, and Swanson

From: Luisa Menchaca, General Counsel
Lawrence T. Woodlock, Senior Commission Counsel

Subject: Proposition 34 Regulations, Allocating Expenditures Subject to Voluntary Expenditure Ceilings, Section 85400. (Proposed Regulation 18540)

Date: September 26, 2001

Introduction

Proposition 34 added to the Political Reform Act ("the Act") a system of Voluntary Expenditure Ceilings. Section 85400 establishes the amount of these ceilings for each of the elective state offices to which an expenditure ceiling is assigned. In campaigns for each office, Section 85400 prescribes one ceiling for primary (or special primary) elections, and a second limit for general, special, or special runoff elections. This memorandum describes proposed Regulation 18540, which would establish guidelines for allocating covered campaign expenditures between and among these elections.

At pre-notice discussion in August, the Commission preferred a regulation that prescribes allocation rules tailored to related classes of campaign expenditures, as presented in subdivision (a). The Commission also opted to include a reference to the appropriate reporting regulation, provisions relating to non-monetary contributions, and a final subdivision identifying expenditures which do *not* count towards the limits prescribed by Section 85400. The four subdivisions of the regulation now before the Commission reflect these earlier choices. Bracketed language at subdivisions (a)(2) and (a)(4) – Decisions 1 and 2 – highlight variations on particular rules that might be useful or necessary under circumstances likely to occur with some frequency.

In addition to the language reviewed at the August meeting, the Commission asked that staff prepare a "fail-safe" provision applicable when operation of a primary allocation rule would otherwise result in misallocation of an expenditure. Decision 3 presents two alternative versions (Options 1 and 2) of such a rule at subdivision (a)(8) of the proposed regulation. This is the only portion of the regulation that the Commission has not seen at the August meeting.

Background

Section 85400(a) provides that: "A candidate for elective state office, other than the Board of Administration of the Public Employees' Retirement System, who voluntarily accepts expenditure limits may not make campaign expenditures in excess of the following:…" The statute then specifies an expenditure limit for primary elections, and a second (higher) limit in post-primary elections, for each of five elective state offices.[1] Because Section 85400 provides separate and distinct limits for every election for each office, to comply with the statute candidates who accept expenditure limits must be able to allocate their expenditures to particular elections.

As amended by SB 34, subdivision (b) of Section 85400 provides that: "For purposes of this section, "campaign expenditures" has the same meaning as "election-related activities" as defined in clauses (i) to (vi), inclusive, and clause (viii) of subparagraph (C) of paragraph (2) of subdivision (b) of Section 82015." Section 82015(b)(2)(C) reads as follows:

> "(C) For purposes of subparagraph (B), a payment is made for purposes related to a candidate's candidacy for elective office if all or a portion of the payment is used for election-related activities. For purposes of this subparagraph, 'election-related activities' shall include, but are not limited to, the following:
>
> (i) Communications that contain express advocacy of the nomination or election of the candidate or the defeat of his or her opponent.
>
> (ii) Communications that contain reference to the candidate's candidacy for elective office, the candidate's election campaign, or the candidate's or his or her opponent's qualifications for elective office.
>
> (iii) Solicitation of contributions to the candidate or to third persons for use in support of the candidate or in opposition to his or her opponent.
>
> (iv) Arranging, coordinating, developing, writing, distributing, preparing, or planning of any communication or activity described in clauses (i), (ii), or (iii), above.
>
> (v) Recruiting or coordinating campaign activities of campaign volunteers on behalf of the candidate.
>
> (vi) Preparing campaign budgets.
>
> (vii) Preparing campaign finance disclosure statements.

[1] The statute separately treats races for the state Assembly, the Senate, for the Board of Equalization, for other statewide offices, and for the governorship.

(viii) Communications directed to voters or potential voters as part of activities encouraging or assisting persons to vote if the communication contains express advocacy of the nomination or election of the candidate or the defeat of his or her opponent."

This non-exclusive list of "election-related activities" forms the working definition of "campaign expenditures" under Section 85400.[2] Staff did not think it possible or necessary to elaborate on the definition of "election-related activities" added as Section 82015(b)(2)(C) in 1997 (Stats. 1997, Ch. 450). The continuing evolution of communications technology and the advertising industry, together with the inventiveness of campaign professionals, insures that there will always be novel expenditures requiring *ad hoc* analysis, defeating any attempt at an exhaustive catalogue of expenditures subject to Section 85400. Experience with the Act's reporting requirements has, in any event, left the regulated community with a practical understanding of what constitutes a "campaign expenditure," with few notable exceptions.[3]

Section 85400 does impose one task unfamiliar to the regulated community, in requiring that campaign expenditures now be assigned to particular elections within a larger campaign (typically a primary and a general election). Accordingly, subdivision (a) of Regulation 18540 articulates rules for allocating these expenditures among elections in a given campaign.

Subdivision (a) : Allocating Expenditures Between Elections

Emergency Regulation 18542 states the manner in which candidates may indicate acceptance or rejection of the new ceilings.[4] The most pressing question that remains is how candidates who accept those limits must allocate their expenditures to the various elections.

Regulation 18540(a) describes six different classes of campaign expenditures which, staff believes, include nearly all typical campaign expenditures. An allocation rule is provided for each class of expenditure. Subdivision (a)(7) then states a "catch-all" or "default" rule providing that expenditures not falling within one of the previously enumerated classes shall be allocated to the next election held on or after the date when the expenditure was made. Subdivision (a)(8) contains alternative versions of the "fail-safe" rule requested by the Commission in August, permitting or requiring candidates to depart

---

[2] There is one exception to this statement. SB 34 has recently modified Section 85400 to remove compliance costs (Section 82015(b)(2)(C)(vii)) from the expenditures subject to Section 85400.

[3] The one common form of "campaign expenditure" that occasionally generates confusion is the "non-monetary" or "in-kind" contribution. The practice in California, as well as in the federal system and in virtually all states, is to regard non-monetary contributions as campaign "expenditures" made on the date of receipt. In August, the Commission decided to expressly state this rule in the proposed regulation, to minimize reporting errors among persons not familiar with a practice that, while necessary, can appear counter-intuitive.

[4] Regulation 18542 will come before the Commission for permanent adoption at the October meeting, when the Commission will also be considering adoption of Regulation 18540.

from the preceding rules whenever those rules would result in misallocation of a campaign expenditure. Subdivision (a)(9) would obligate candidates to maintain records supporting their expenditure allocations.

A closely related provision, subdivision (b), would require that allocations under Section 85400 be reported on the campaign reports due on or after the date the expenditure is made.

Subdivision (a) is modeled on a corresponding federal regulation (11 CFR Section 106.2, allocation of expenditures in presidential elections subject to expenditure ceilings), adapted to reflect the kinds of expenditures commonly reported as campaign expenditures in California. It is designed to assist the reader in identifying the rule applicable to coherent classes of campaign expenditures. The importance of tailoring allocation rules to classes of expenditure is illustrated throughout the proposed regulation. The default rule would attribute expenditures to the election immediately following the point at which the expenditure is made. But that rule would allocate to a primary election money spent early in the campaign to reserve television time for an advertising blitz on the eve of the *general* election. In subdivision (a)(2), the date of publication or distribution of such advertisements determines the election to which the expenditure will be allocated. Fundraising is another common example of expenditures often made far in advance of the election which they are intended to influence. Under subdivision (a)(6), fundraising costs are allocated wherever possible to the election for which the funds are raised.

Bracketed language in subdivision (a)(4) (**Decision 1**) would cover instances where a contract for professional services expressly allocates fees and costs to particular elections. This language would provide that the terms of the contract will determine how the expenditures will be allocated. This provision would allow services to be allocated more accurately, especially in contracts which obligate the candidate for the entire contract payment on the date the contract is signed, which require large pre-payments or, conversely, which defer payment obligations to a later date. On the other hand, it is possible that this additional language would permit "gaming" of the rules, transferring to the parties a degree of control that would encourage grossly unrealistic expenditure allocations. Staff has no recommendation on this point.

In other expenditure classes it is less common to spend large sums of money during one pre-election period for goods or services disseminated in another election. This is typically the case with telephone banks, professional services, and overhead expenses, for example.

Bracketed language not considered by the Commission at the last meeting (**Decision 2**) would add to subdivision (a)(7) a rule governing refunds of expenditures for goods or services not provided to or used by the campaign. Although this language was not included in subdivision (a)(7) when the regulation came before the Commission for prenotice discussion in August, a similar provision was included as an option in subdivision (a)(2), where it was limited to refunds for broadcast advertisements.[5] There is no real ground for so narrowly limiting a "refund rule," and staff has therefore removed the specialized rule from subdivision (a)(2), and replaced it with a more general provision in subdivision (a)(7).

This provision requires allocation of refunds to the election for which the payment would otherwise have been allocated. Thus, a candidate who chose to exceed an expenditure ceiling in an unexpectedly close primary campaign would not be able to escape the consequences of that choice after losing in the primary, by taking a refund of advertising dollars allocated to the general election and applying it *post hoc* to bring primary expenditures down to a permissible level. Staff recommends adoption of this proviso.

Decision 3, ***The New "Fail-Safe" Rule of Subdivision (a)(8)***

There is little doubt that strict application of the rules contained in the first seven sections of subdivision (a) could, at times, result in misallocation of expenditures to the "wrong" election, due to any number or combination of circumstances within a given campaign. Any finite set of rules would share this defect. For that reason, at the August meeting the Commission directed staff to fashion a provision that would permit or require candidates to adjust their allocations to match the real-world effects of their campaign expenditures, when application of another rule would result in misallocation. Staff has prepared two such provisions. **Option 1** is a brief, general rule which presumes that the intent of Section 85400 is to allocate expenditures to the elections whose outcomes they actually influence. Since many expenditures in a primary election would have some degree of "carryover" effect on the general, this rule addresses expenditures which "would operate *primarily* to influence the voters in an election other than the election to which the expenditure is allocated under the foregoing rules."

Some degree of subjectivity is implicit in the term "primarily," but precision in measuring the effects of campaign spending can rarely be achieved. The rule is not intended to operate in marginal cases where the actual effect of an expenditure is fairly debatable, but should be invoked when it is clear that application of subdivisions (a)(1) through (a)(7) would result in allocation to an election only incidentally affected by the expenditure. The same considerations animate the second sentence of this proposed rule, requiring apportionment of expenditures "made, or intended, to influence two or more elections."

The bracketed alternatives ("may" as against "shall," **Options 1a and 1b**) invite the Commission to decide whether this "fail-safe" rule should be mandatory or permissive. If the rule is mandatory, campaigns would be forced at times to make difficult "calls" on the effects of their expenditures, possibly guessing incorrectly on occasion and opening the door in any event to challenges

---

[5] The noticed version of this regulation included the following sentence at the end of subdivision (a)(2): "Refunds for broadcast time or advertisement space, purchased but not broadcast, published, or disseminated, shall be credited to the election for which the expenditure would otherwise have been allocated."

and second-guessing. If the rule were permissive, the same dangers would attend campaigns that chose to invoke it, *and* a free choice of rules would present a new opportunity for strategic behavior probably not intended by Section 85400. On balance, if the Commission chooses Option 1, staff recommends that the rule be mandatory.

Option 1c is would provide that expenditures made to influence the outcome of a primary election may not be allocated to a general election on the ground that success in the primary effectively dictates the outcome in the general election, a commonplace in many jurisdictions.

Option 2 offers a more narrow alternative, focused on the anticipated use of goods or services, when that expected use is plainly documented.[6] Because its application is confined to readily documented circumstances, there is little to fear from making such a rule mandatory. The Enforcement Division strongly prefers this Option, since the rule must be followed in clearly specified circumstances. The Legal Division is concerned that the specificity which makes enforcement simple also defeats the purpose of a "fail-safe" rule, to the extent that expenditures will still be misallocated whenever the specified criteria are not met.[7] The more specific the criteria (**Options 2a** and **2b** add further specificity), the more occasions on which the rule will not be applied, and misallocation tolerated.

Staff has considered the possibility of an option that combines the two approaches, but such an option appears to be infeasible. Specific rules akin to Option 2, added to a general rule like Option 1, would add nothing not plainly required and easily enforced under the general rule.

At the same time, in cases where the general rule was difficult to enforce, no benefit would attach from the addition of rules applicable only to easier cases. The Commission cannot avoid the fundamental question; does it wish to enact a provision applicable in every case where an expenditure would otherwise be misallocated, although it might be hard to enforce in close cases, or does it prefer a narrow, more easily enforced rule that could not address all instances where expenditures would be misallocated? Staff has no firm recommendation as between Option 1 and Option 2.

Subdivision (b)

Subdivision (b) directs the reader to Emergency Regulation 18421.4(b), which prescribes the manner in which allocations under Section 85400 shall be reported.[8]

---

[6] Option 2 also includes a rule applicable to goods or services left over after the election to which they were allocated, but used instead in a subsequent election. This rule applies by its terms to a small subclass of expenditures, although within that narrow range it operates as a general rule.

[7] For example, a quantity of bumper stickers optimistically purchased late in the primary period for distribution during the general election period, which say only "Candidate X for Mayor," would be misallocated under subdivision (a)(1) to the primary election, an outcome that would *not* change under Option 2 if the purchase order did not "clearly identify the election for which the goods are intended be be used."

[8] Regulation 18421.4, like all emergency regulations pertinent to proposed Regulation 18540, will come before the

Subdivision (c): Non-Monetary Contributions

Sections 85400 and 82015(b)(2)(C) do not consider the *form* that expenditures may take, and so have nothing to say about the "in-kind" or "non-monetary" contribution. Candidates with reporting obligations under the Act currently report non-monetary contributions as "expenditures" on the summary page of their Forms 460, and the treatment of non-monetary contributions as the functional equivalent of "expenditures" is well established under the Act. Jurisdictions with expenditure ceilings (now including California) have a particular interest in characterizing "non-monetary contributions" as "expenditures," both for accurate accounting, and to discourage evasion of expenditure limits by replacement of monetary with non-monetary contributions.

Regulation 18540(c) follows many local California jurisdictions in expressly stating that non-monetary contributions will count as "expenditures" subject to expenditure limits.[9]

The fundamental reason for including in this regulation an express provision relating to non-monetary contributions is notice to persons who may not be familiar with the nature and use of non-monetary contributions who, misled by terminology, may not grasp their real-world equivalence with campaign expenditures. "Contribution" and "expenditure" are normally viewed as opposites, like "giving" and "receiving." This distinction is satisfactory, however, only when the contribution comes in the form of money. An example will illustrate the peculiar features of non-monetary contributions, which are not always understood by the public.

If a contributor provided a check for $1,000 to a campaign on Monday, that check could be deposited in the campaign bank account and recorded the same day as a contribution. On Tuesday, the treasurer could make out a $1,000 check on the same account, to pay for a quantity of campaign mailers, whereupon the treasurer would enter a $1,000 expenditure on the books. Contribution and expenditure are duly recorded, and the expenditure would count against an expenditure ceiling. To prevent evasion of expenditure ceilings, the result must be the same when the contributor takes his check on Monday to the printer and purchases the campaign mailers himself, delivering the mailers to the campaign on Tuesday as a non-monetary contribution. To insure that the consequences are the same regardless of *who* purchases the mailers, the non-monetary contribution is treated as both contribution *and* expenditure. Although it is the *contributor* who makes the expenditure, he does so on behalf of the campaign.

If the contribution of $1,000 worth of mailers did not count against campaign expenditure limits, jurisdictions employing such limits would find that, instead of moderating the costs of political

---

Commission for permanent adoption in October, when Regulation 18540 will also be up for adoption.

[9] For example, Long Beach, Los Angeles and San Francisco have, or have had, ordinances defining "Qualified Campaign Expenditures" to include "A non-monetary contribution provided at the request of or with the approval of the candidate, officeholder or [committees variously identified]."

campaigns, expenditure limits would inevitably cause a migration away from monetary contributions in favor of less readily documented transactions that would allow the costs of campaigns to soar beyond the statutory limits. This, in a nutshell, is why jurisdictions with expenditure ceilings characterize non-monetary contributions as *de facto* expenditures.

The Commission has previously decided to include Subdivision (c) in this regulation.

Subdivision (d): Listing Expenditures That Do Not Count Against the Limits

Subdivision (d) identifies certain expenditures that will not be subject to the voluntary expenditure ceilings of Section 85400. The "exceptions" listed in this subdivision are based on provisions of the Act or existing regulations. It is staff's experience that the public is often uncertain how to characterize or report these expenditures, and the Commission decided at the August meeting to include this provision in the regulation.